

THE HONORABLE RICHARD A. JONES

UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF WASHINGTON
AT SEATTLE

SEATTLE CITY EMPLOYEES'
RETIREMENT SYSTEM, an agency of the
City of Seattle,

Plaintiff,

v.

EPSILON GLOBAL ACTIVE VALUE FUND
II, LTD., a British Virgin Islands corporation,
EPSILON GLOBAL MASTER FUND II, L.P.,
a limited partnership formed under the laws of
the Cayman Islands, EPSILON INVESTMENT
MANAGEMENT, LLC, a Delaware limited
liability company, EPSILON GLOBAL ASSET
MANAGEMENT LTD., a corporation formed
under the laws of the Cayman Islands, and
STEVEN G. STEVANOVICH, a resident of
Florida,

Defendants.

No. 2:10-cv-555

DEFENDANTS' ANSWER AND
AFFIRMATIVE DEFENSES

ANSWER

Defendants Epsilon Global Active Value Fund II, Ltd. ("Epsilon II"), Epsilon Global
Master Fund II, L.P. ("Epsilon Master Fund II"), Epsilon Investment Management, LLC
("Epsilon Investment Management"), Epsilon Global Asset Management Ltd. ("Epsilon Asset
Management"), and Steven G. Stevanovich (collectively "Defendants") answer Plaintiff's

DEFENDANTS' ANSWER
(NO. 2:10-CV-555) – 1

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Seattle, WA 98101-3099
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1 Complaint as follows, in paragraphs numbered to correspond to the paragraph numbers in said
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3 Complaint:

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5 **I. PARTIES**

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7 1. As to paragraph 1, Defendants admit that Plaintiff is an agency of the City of
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9 Seattle that provides retirement, disability, and survivors' benefits to City of Seattle employees,
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11 and which is administered in Washington state. Except as so expressly admitted, Defendants
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13 have insufficient information to admit or deny the remaining allegations of paragraph 1 and on
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15 that basis deny these allegations.

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17 2. As to paragraph 2, Defendants admit that Epsilon II is a British Virgin Islands
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19 private investment corporation, that Mr. Stevanovich is a director of Epsilon II involved in
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21 directing its operations, and that Monahan & Biagi, PLLC, is located in Seattle and acts as legal
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23 counsel to Epsilon II. Except as so expressly admitted, Defendants deny the allegations in
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25 paragraph 2.

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27 3. As to paragraph 3, Defendants admit that Epsilon Master Fund II is a limited
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29 partnership formed under the laws of the Cayman Islands, that proceeds from the sale of shares
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31 in Epsilon II are invested into Epsilon Master Fund II, and that Epsilon II's financial position is
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33 directly tied to Epsilon Master Fund II. Defendants further respond that Mr. Stevanovich is the
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35 director of Epsilon Asset Management, which is general partner of Epsilon Master Fund II, and
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37 therefore Mr. Stevanovich is involved in directing Epsilon Master Fund II's activities. Except as
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39 so expressly admitted, Defendants deny the allegations in paragraph 3.

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41 4. As to paragraph 4, Defendants admit that Epsilon Asset Management is a Cayman
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43 Islands corporation that is general partner of Epsilon Master Fund II and that Epsilon Asset
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45 Management is former investment manager of Epsilon II, at which time it was solely responsible
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47 for trading and investment decisions of Epsilon II. Defendants further respond that Mr.
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49 Stevanovich is the director of Epsilon Asset Management and that he was involved in Epsilon
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1 II's trading and investment decisions when Epsilon Asset Management was investment manager
2 of Epsilon II. Except as so expressly admitted, Defendants deny the allegations in paragraph 4.
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4 5. As to paragraph 5, Defendants admit that Epsilon Investment Management is a
5 Delaware limited liability company and current investment manager for Epsilon II that provides
6 analysis and recommendations related to Epsilon II's trading and investment transactions.
7 Defendants further admit that Mr. Stevanovich is founder, president, CFO, and sole manager of
8 Epsilon Investment Management and is therefore involved in trading and investment decisions.
9 Defendants also admit that Epsilon Investment Management communicates with Plaintiff with
10 respect to Plaintiff's investment in Epsilon II. Except as so expressly admitted, Defendants deny
11 the allegations in paragraph 5.
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13 6. As to paragraph 6, Defendants admit that Mr. Stevanovich resides in Delray
14 Beach, Florida, is a director of Epsilon II and Epsilon Asset Management (the latter being
15 general partner of Epsilon Master Fund II), and therefore Mr. Stevanovich is involved in
16 directing Epsilon II's and Epsilon Master Fund II's activities. Defendants further admit that Mr.
17 Stevanovich is manager of Epsilon Investment Management and therefore is involved in trading
18 and investment decisions. Except as so expressly admitted, Defendants deny the allegations in
19 paragraph 6.
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21 7. As to paragraph 7, Defendants have insufficient information to admit or deny the
22 allegations of paragraph 7 and on that basis deny these allegations.
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24 II. JURISDICTION AND VENUE

25 8. As to paragraph 8, Defendants admit that Plaintiff received materials soliciting its
26 investment in Epsilon II. Except as so expressly admitted, Defendants deny the allegations in
27 paragraph 8.
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29 9. As to paragraph 9, Defendants admit that King County Superior Court had subject
30 matter jurisdiction over the action. Defendants further respond that the United States District
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1 Court for the Western District of Washington has subject matter jurisdiction on the basis of
2 diversity. Except as so expressly admitted, Defendants deny the allegations in paragraph 9.
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4 10. As to paragraph 10, Defendants admit that venue was proper in King County
5 Superior Court. Defendants further respond that venue is proper in United States District Court
6 for the Western District of Washington. Except as so expressly admitted, Defendants deny the
7 allegations in paragraph 10.
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10 III. FACTS

11 11. As to paragraph 11, Defendants admit that Plaintiff received materials soliciting
12 its investment in Epsilon II. Except as so expressly admitted, Defendants deny the allegations in
13 paragraph 11.
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15 12. As to paragraph 12, Defendants admit that Plaintiff received materials soliciting
16 its investment in Epsilon II. Defendants further admit that a copy of the January 2003
17 Confidential Offering Memorandum is attached as Exhibit A to the Complaint. Except as so
18 expressly admitted, Defendants deny the allegations in paragraph 12.
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20 13. As to paragraph 13, Defendants admit that, in or about December 2003, Plaintiff
21 purchased \$10 million in shares in Epsilon II by accepting the terms offered in the January 2003
22 Confidential Offering Memorandum and executing a Subscription Agreement and Standing
23 Proxy. Defendants further admit that Plaintiff purchased an additional \$10 million in shares
24 approximately one year later. Defendants further respond that the second investment occurred in
25 or about December 2004. Except as so expressly admitted, Defendants deny the allegations in
26 paragraph 13.
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28 14. As to paragraph 14, Defendants respond that the January 2003 Confidential
29 Offering Memorandum speaks for itself. Defendants further respond that paragraph 14 asserts a
30 legal conclusion, to which no response is required.
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1 15. As to paragraph 15, Defendants respond that the January 2003 Confidential
2 Offering Memorandum speaks for itself. Defendants further respond that paragraph 15 asserts a
3 legal conclusion, to which no response is required.
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6 16. As to paragraph 16, Defendants admit that historically, annual reports with
7 financial statements for Epsilon II have been provided to Plaintiff. Except as so expressly
8 admitted, Defendants deny the allegations in paragraph 16.
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11 17. As to paragraph 17, Defendants admit that Epsilon II did not provide Plaintiff
12 with a 2008 annual report with audited financial statement by May 1, 2009. Defendants further
13 respond that paragraph 17 asserts a legal conclusion for which no response is required. To the
14 extent a response is required, except as so expressly admitted, Defendants deny the allegations in
15 paragraph 17.
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18 18. As to paragraph 18, Defendants admit that Plaintiff inquired about the status of
19 the 2008 annual report with audited financial statement. Defendants further admit that Epsilon
20 Investment Management informed Plaintiff that the 2008 annual report with audited financial
21 statement would be forthcoming once Pricewaterhouse Coopers ("PwC") completed and released
22 the audit. Except as so expressly admitted, Defendants deny the allegations in paragraph 18.
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24 19. As to paragraph 19, Defendants admit the allegations therein. Defendants further
25 respond that, as of the date hereof, the 2008 annual report with audited financial statement
26 cannot be provided because PwC has not completed and released the audit.
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28 20. As to paragraph 20, Defendants admit that on or about January 28, 2010, Plaintiff
29 notified Epsilon Investment Management that Plaintiff would like to redeem its shares in
30 Epsilon II. Defendants further admit that on February 4, 2010, Epsilon Investment Management
31 announced the temporary suspension of redemptions in three funds, including Epsilon II.
32 Defendants further respond that a copy of the February 4 memorandum ("Memorandum") is
33 attached as Exhibit C to the Complaint, and the Memorandum speaks for itself. To the extent a
34 response is required, Defendants further admit that the Memorandum references an SEC
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1 investigation into Westford I, a lack of liquidity (particularly affecting Westford I), and the fact
2 that PwC informed Defendants that completion and release of audited financial statements would
3 be delayed because of the SEC investigation. Except as so expressly admitted, Defendants deny
4 the allegations in paragraph 20.
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8 21. As to paragraph 21, Defendants admit the allegations therein. Defendants further
9 respond that a copy of the referenced email is attached as Exhibit D to the Complaint, and the
10 email speaks for itself.
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14 22. As to paragraph 22, Defendants admit that Exhibit E to the Complaint is an
15 "Investor Statement" showing Plaintiff's Epsilon II account summary for the period December
16 2009, which document speaks for itself. To the extent a response is required, Defendants further
17 respond that the Investor Statement was provided by Equinox, administrator of the Epsilon II
18 fund. Defendants deny that the statement indicates a closing position of \$24,865,756.33 (rather,
19 it indicates \$24,856,756.33). Except as expressly admitted, Defendants have insufficient
20 information to admit or deny the allegations in paragraph 22 and on that basis denies all
21 remaining allegations therein.
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25 23. As to paragraph 23, Defendants admit that Exhibit F to the Complaint is a copy of
26 an email sent to Epsilon Investment Management on or about March 8, 2010, which document
27 speaks for itself.
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30 24. As to paragraph 24, Defendants incorporate their response to paragraph 23 above.
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32 25. As to paragraph 25, Defendants admit that a representative of Plaintiff sent a
33 March 8, 2010, email demanding a meeting in Seattle on March 15, 2010, and that
34 representatives of Defendants were unable to travel to Seattle for the requested meeting on such
35 short notice. Except as so expressly admitted, Defendants deny the allegations in paragraph 25.
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38 26. As to paragraph 26, Defendants deny the allegations therein.
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40 27. As to paragraph 27, Defendants respond that Exhibit G to the Complaint is a copy
41 of the Epsilon II "Directors' report and financial statements for the year ended December 31,
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2007," which document speaks for itself. To the extent a further response is required, Defendants admit that the referenced 2007 report indicates that "Net assets attributable to holders of redeemable participating shares" was \$24,222,405 (as of December 31, 2007). As to the remaining allegations in paragraph 27, Defendants incorporate by reference their response above to paragraph 22.

28. As to paragraph 28, Defendants deny the allegations therein.

29. As to paragraph 29, Defendants admit that Mr. Stevanovich is involved, in various capacities, in the operations of Epsilon Investment Management, Epsilon Asset Management, and Epsilon Master Fund II. Defendants further admit that "Defendant . . . Stevanovich . . . [is] controlled by [Defendant] Stevanovich." Except as expressly admitted, Defendants deny the allegations in paragraph 29.

30. As to paragraph 30, Defendants admit that Mr. Stevanovich is a director of Epsilon II and is therefore involved in directing its operations and activities. Defendants also admit that Mr. Stevanovich is manager of Epsilon Investment Management and therefore is involved in its trading and investment decisions. Defendants further respond that Mr. Stevanovich is the director of Epsilon Asset Management, which is general partner of Epsilon Master Fund II, and therefore Mr. Stevanovich is involved in directing Epsilon Master Fund II's activities. Except as expressly admitted, Defendants deny the allegations in paragraph 30.

31. As to paragraph 31, Defendants admit that the February 4, 2010, memorandum to shareholders announcing the suspension of redemptions in Epsilon and Westford funds was written on Epsilon Investment Management letterhead and signed by Mr. Stevanovich. Defendants further respond that the February 4 memorandum speaks for itself. Except as expressly admitted, Defendants deny the allegations in paragraph 31.

32. As to paragraph 32, Defendants admit that Mr. Stevanovich is involved in directing the operations of the Defendant Epsilon entities. Defendants further respond that PwC has not completed and released the 2008 annual report with audited financial statement and

1 therefore it cannot be produced. Except as expressly admitted, Defendants deny the allegations
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3 in paragraph 32.

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5 **V. CAUSES OF ACTION**

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7 **First Claim for Relief**

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9 **Breach of Contract**

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11 33. As to paragraph 33, Defendants incorporate their responses to paragraphs 1
12 through 32 as though fully set forth herein.

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14 34. As to paragraph 34, defendants deny the allegations therein.

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16 35. As to paragraph 35, defendants deny the allegations therein.

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18 **Second Claim for Relief**

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20 **Violation of British Virgin Islands Business Companies Act of 2004**

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22 36. As to paragraph 36, Defendants incorporate their responses to paragraphs 1
23 through 35 as though fully set forth herein.

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25 37. As to paragraph 37, Defendants respond that it asserts a legal conclusion, to
26 which no response is required.

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28 38. As to paragraph 38, Defendants respond that the referenced offering
29 memorandum speaks for itself. Defendants further respond that paragraph 38 asserts a legal
30 conclusion, to which no response is required.

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32 39. As to paragraph 39, Defendants admit that Epsilon II has yet to provide Plaintiff
33 with the 2008 annual report with audited financial statement. Defendants further respond that
34 PwC has not completed and released the 2008 annual report with audited financial statement and
35 therefore it cannot be produced. Except as expressly admitted, Defendants deny the allegations
36 in paragraph 39.

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Third Claim for Relief

Injunctive Relief Requiring Production of Financial Documents

40. As to paragraph 40, Defendants incorporate their responses to paragraphs 1 through 39 as though fully set forth herein.

41. As to paragraph 41, defendants deny the allegations therein.

42. As to paragraph 42, defendants deny the allegations therein.

43. As to paragraph 43, defendants deny the allegations therein.

44. As to paragraph 44, defendants deny the allegations therein.

Fourth Claim for Relief

**Injunctive Relief Preventing Epsilon II from Taking Action Harmful
to SCERS as an Investor or Its Investment**

45. As to paragraph 45, Defendants incorporate their responses to paragraphs 1 through 44 as though fully set forth herein.

46. As to paragraph 46, defendants deny the allegations therein.

Fifth Claim for Relief

**Injunctive Relief Preventing Epsilon II from Paying Any Management Fee
During the Gating of SCERS's Investment**

47. As to paragraph 47, Defendants incorporate their responses to paragraphs 1 through 46 as though fully set forth herein.

48. As to paragraph 48, defendants deny the allegations therein.

AFFIRMATIVE DEFENSES

Defendants further respond to Plaintiff's Complaint by alleging the following affirmative defenses:

1. Plaintiff's Complaint fails to state a claim upon which relief may be granted.
2. The Court lacks personal jurisdiction over Defendants.

1 3. Service of process on Defendants Epsilon II, Epsilon Master Fund II, and Epsilon
2 Asset Management was insufficient.

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4 4. Plaintiff's claim, in part, is brought prematurely and is not actionable.

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6 5. Defendants' contractual obligations were not due because of the nonoccurrence of
7 a necessary condition to performance.

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9 6. Defendants' contractual obligations are excused based on the doctrines of
10 impossibility and/or impracticability.

11 7. Plaintiff's claim is barred by the equitable doctrine of laches.

12 8. Plaintiff is estopped from asserting the claim against Defendants.

13 9. Plaintiff has waived its rights against Defendants and is not entitled to relief.

14 10. The requested injunctive relief is unavailable because Plaintiff has an adequate
15 remedy at law.

16 11. The relief sought by Plaintiff is not available under the law of the British Virgin
17 Islands, which is the applicable substantive law in this action.

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29 **PRAYER FOR RELIEF**

30 WHEREFORE, Defendants demand the following relief:

31 A. Dismissal of Plaintiff's claims with prejudice;

32 B. Defendants' costs of suit, including reasonable attorneys' fees; and

33 C. Such other relief as the Court may deem just and proper.
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1 DATED this 14th day of April, 2010.
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s/ Joseph M. McMillan

Harry H. Schneider, Jr., WSBA No. 09404

Joseph M. McMillan, WSBA No. 26527

Jeffrey M. Hanson, WSBA No. 34871

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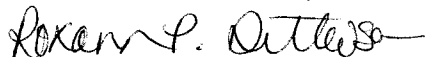
CERTIFICATE OF SERVICE

On the 14th day of April, 2010, I caused to be served upon the following, at the address stated below, via the method of service indicated, a true and correct copy of the foregoing document.

Bradley P. Thoreson	<input type="checkbox"/>	Via hand delivery
Samuel T. Bull	<input type="checkbox"/>	Via U.S. Mail, 1st Class,
Miriam H. Cho		Postage Prepaid
Foster Pepper PLLC	<input checked="" type="checkbox"/>	Via CM/ECF system
1111 Third Avenue, Suite 3400	<input type="checkbox"/>	Via Overnight Delivery
Seattle, WA 98101	<input type="checkbox"/>	Via Facsimile
thorb@foster.com	<input checked="" type="checkbox"/>	Via Email
bulls@foster.com		
chomi@foster.com		

I certify under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct.

DATED at Seattle, Washington, this 14th day of April, 2010.


Roxann P. Ditlevson